

2300 N Street, NW
Suite 600
Washington, DC 20037
Phone 202/663-9060
Fax 202/663-9065

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Robert E. Lloyd
Vice President
Government Relations

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

December 16, 1994

Mr. Bill Caton
Acting Secretary
Federal Communications Commission
Room 222
1919 M Street, N.W.
Washington, D.C. 20554

Re: Safeguards to Improve
the Administration of Interstate
Access Tariff and Revenue
Distribution Processes

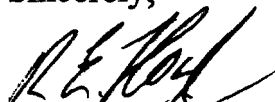
Written Ex Parte Notice
CC Docket No. 93-6

Dear Mr. Caton:

On December 15, 1994, NECA representatives Bruce Baldwin, Ken Levy and Robert E. Lloyd met with Common Carrier Bureau staff members Bill Kehoe, Kathleen Levitz, John Hays and John Morabito to discuss the NECA Safeguards Notice of Proposed Rulemaking. (see attached).

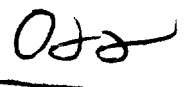
Please acknowledge receipt hereof by affixing a notation on the duplicate copy of this letter furnished herewith for such purposes and remitting same to bearer.

Sincerely,


Robert E. Lloyd

cc: B.Kehoe J.Morabito
K. Levitz
J.Hays

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SAFEGUARDS TO IMPROVE THE ADMINISTRATION OF THE INTERSTATE ACCESS TARIFF AND REVENUE DISTRIBUTION PROCESSES

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the spring of 1989, the Federal Communications Commission ("FCC" or "Commission") commenced a survey audit of the National Exchange Carrier Association, Inc. ("NECA"). This audit focused on the settlement process and certain adjustments to the Common Line Pool during the last quarter of 1988. On November 9, 1990, in response to the audit's findings that certain improper pool reporting transactions had taken place, the Commission issued four Notices of Apparent Liability to individual Bell Operating Companies and a letter to the NECA Board of Directors. Pursuant to FCC directives, NECA hired an independent auditor, Ernst & Young (E&Y) to review certain Common Line Pool adjustments for 1988 and 1989 and to recommend safeguards to prevent future occurrences of improper transactions.

On December 9, 1991, NECA filed two detailed reports with the FCC. The first was an E&Y report which evaluated the aforementioned Subset I Common Line Pool adjustments. The second was an E&Y report on additional safeguards that could be implemented, as well as NECA responses to these recommendations. As NECA Chairman Ware stated in his December 9, 1991, letter to the Commission, "E&Y noted that substantial changes in NECA's pooling environment and operations have occurred since the Common Line Pool became voluntary in April 1989, and that a number of important safeguards have evolved as a result of these changes."

NECA's response to the Safeguards Report showed that it had voluntarily taken several initiatives to respond to Commission concerns prior to the issuance of the E&Y report. For example, NECA obtained the necessary waivers to conduct an election of two "outside" directors for its 1992 Board and to allow these directors to participate in the Board pooling committees. Two outside directors participate in the critical Universal Service/Lifeline Board Committee. In addition, NECA formalized its requirements for the creation and ongoing operation of Board subcommittees, by revising its By-laws. Explicit statements of NECA Board and staff responsibilities for compliance with Commission rules have been adopted. Recently, the NECA Board adopted an open outside director election and nomination process.

On February 11, 1993, the Commission released a Notice of Proposed Rulemaking ("NPRM") to improve NECA's administrative processes. In the NPRM, the FCC acknowledged NECA's significant procedural improvements since the beginning of the audit. According to the FCC, the proposed safeguards would enable NECA to add to its record of achievement in administering the interstate access tariff and revenue distribution processes.

In comments filed on April 14, 1993, NECA demonstrated that its procedures ensure compliance with Commission rules. Exchange carriers, consultants, and associations,

including the National Association of Regulatory Utility Commissioners (NARUC), supported NECA's excellent record in reply comments filed on May 14, 1993. The majority of commenting parties concur with NECA's proposals.

The following outline identifies the principal issues raised in the NPRM and what the record reflects regarding the proposed additional NECA safeguards.

I. NECA'S BOARD OF DIRECTORS

A. Inclusion of Outside Director's on NECA's Board

1. The proposal to amend Section 69.602 of the Commission's rules to add two (2) outside directors permanently to the NECA Board should be adopted.
 - a. NECA first added two (2) outside directors to its Board in 1992 under FCC waiver and that waiver has been extended through 1994.
 - b. The addition of the outside directors has proven beneficial, and has "provided a valuable non-industry perspective to the Board decisionmaking process."
2. All parties commenting on this issue agreed that the addition of two outside directors should be made permanent. Although GCI went further and stated that NECA should add three outside directors, it did not provide any reasons for its proposal. The record does not support the addition of more than two outside directors at this time.

B. Overall Composition of Board

1. The current Board size and composition are working well and there is no cause for a change in representation.
 - a. The Board's composition has been finely tuned over the last nine (9) years to reflect the delicate balance of EC interests on the NECA Board as it has evolved.
 - b. The current structure assures fair representation of NECA

members and provides the benefit of outside opinions

- (1) Three (3) Subset I directors represent the seven (7) RBOCs
 - (2) Three (3) Subset II directors represent twenty-two (22) companies, which include mid-sized and holding companies for a number of smaller telephone companies.
 - (3) Nine (9) Subset III directors represent nine-hundred thirty-nine (939) diverse companies, which include average schedule companies, cost companies, companies that have from less than one hundred (100) lines to upwards of fifty thousand (50,000) lines, REA borrowers and non-REA borrowers, high cost and low cost companies, co-ops, investor and family-owned companies, municipally and tribal-run companies, rural area companies, and ECs that serve urban and suburban areas.
 - (4) Two (2) outside directors contribute a non-industry perspective to the NECA Board.
2. The record does not support a change in Board composition. Only one commenter, Ameritech, suggested changing the current NECA Board size and composition, by reducing it from seventeen (17) to eleven (11) members. Ameritech's rationale for this change is faulty in that it presumes that the number of issues before the Board have been reduced because, among other things, the Traffic Sensitive Pool membership has decreased. NECA has not found this decline in issues to be the case. There was no support for Ameritech's proposal from other commenters.

C. Eligibility Criteria

1. NECA recommends the adoption of its suggested eligibility criteria under which "current or former officers or employees of NECA or any of its members are ineligible for outside directorships," and "outside directors may not have business relationships, family relationships, or other interests that could interfere with their judgment."

- a. Under NECA's criteria, a pool of outside director candidates would consist of members of the business, professional, financial, and academic communities, as well as former government officials.
 - b. In the NPRM, the FCC tentatively concluded that the eligibility criteria proposed by NECA met its objectives.
 - c. A slight modification from NECA's original language affords NECA the flexibility to consider qualified nominees whose family relationships would not interfere with their judgment as an outside director
2. NECA's eligibility criteria enjoy general industry support.
- a. No oppositions to NECA's original criteria or its slight modification was registered.
 - b. Several commenters stated that NECA should retain latitude to fine tune eligibility criteria as needed and recommended that specific detailed rules not be adopted.

D. Selection of Outside Directors and Terms of Office

- 1. NECA's current nomination and annual election procedures for all directors have proven to be effective and are consonant with FCC goals.
- 2. NECA's nomination and election criteria for subset and outside directors render multiple candidates and two-year staggered terms unnecessary.
 - a. Directorship rotation for Subset I and Subset II companies, and the open nomination process for Subset III companies have successfully resulted in diverse representation as well as the continuity of experienced board members sharing their knowledge with board newcomers.
 - b. Interim annual uncontested elections for outside directors promote smooth progression of board member training and

reflect uncontested public corporate board elections

- c. Contested outside director elections every three (3) years, or upon an unforeseen vacancy, produce a balanced board that combines experience and continuity with ample turnover of board members.
3. Given the turnover rate of NECA's Board, term limitations are unnecessary and should not be imposed by the FCC.
- a. The FCC did not request term limitations in its NPRM proposals.
 - b. The Board's turnover rate, moreover, promotes continuity, resident expertise, and the influx of new ideas.
 - c. The National Telephone Cooperative Association (NTCA), Bell Atlantic, and ICORE, Inc. agree with NECA that mandatory term limitations are unnecessary and should not be adopted. Ameritech was the only commenter to propose term limitations but provided no rationale for such a change. Again commenters stated that procedures such as election and nomination of outside directors should be left to the discretion of NECA within the parameters it has proposed to the Commission.

E. Voting Privileges on Committees

In accordance with the FCC's recommendation, NECA has already placed outside directors on each Board committee, including the Common Line and Traffic Sensitive Committees, pursuant to FCC waiver.

F. Formalization of Board Committee Requirements

Responding to the FCC's concern over committee structure and rules, NECA amended its by-laws to provide procedures and requirements for the appointment and operation of Board subcommittees.

II. NECA RESPONSIBILITIES UNDER COMMISSION RULES

A. NECA's Overall Responsibilities

1. NECA's procedures and corporate policies reflect its commitment to FCC rule compliance.
2. E&Y found that compared to those in place in 1988, NECA had "significantly enhanced the safeguards against potential manipulation of pooling information."
3. NECA continues to make substantial efforts to improve cost study review and validation procedures.
 - a. NECA has instituted manual and mechanized "streamlined" cost study validations on all of its cost company study areas.
 - b. NECA redesigned its validation process as a Cost Analysis Program.
 - c. NECA revised and enhanced the Cost Analysis Procedures in 1992, which are updated quarterly.
 - d. Introduction of Focused Cost Study Reviews concentrate on FCC rule compliance in specific priority subject areas.
 - e. NECA has improved its Detailed Cost Study Review Procedures to validate the streamlined cost study review process and to identify risk areas.
 - f. NECA's Cost Issues Resolution Process has been substantially supplemented since the independent auditor conducted the safeguards review. The purpose of NECA's Cost Issues Manual is to provide a source for uniform treatment of issues in compliance with the Commission's rules and orders to ensure equitable settlements among NECA pool members. This process includes the gathering of data and circulating issues among the members as well as early referral of issues to the Commission.
4. NECA's handling of cost study issues garnered general support from commenting parties.

B. On-line Access to NECA Data Bases

1. On-line, dial-up access to NECA's computer based files is unwarranted and should not be required by the FCC.
2. Access to NECA's computer based files would not be useful since most of the data is preliminary or estimated.
 - a. Misunderstandings and inaccuracies would be created because the data undergoes continual updates and revisions until it is finalized.
 - b. NECA already provides the FCC with USF, network usage, and tariff cost and demand data on diskette.
 - c. NECA has responded quickly to FCC requests for electronic or written information.
3. Larger ECs are not required to provide on-line access, and imposing such a requirement on NECA pool members would be inequitable and an extraordinary departure from established carrier/regulatory agency arrangements.
4. Out of sixteen commenters, only three, AT&T, GCI and ICORE, voiced support for the FCC's proposal for on-line, dial-up access to NECA's computer based files. NECA has, in the past, provided the Commission with any data required for its review and would continue to accommodate specific requests as the Commission deems necessary. The Commission should not re-write its rules regarding cost support data for tariff filings in this proceeding.

III. STRENGTHENING NECA'S INTERNAL PROCEDURES

A. Monitoring Commission Developments/Certification of Cost Study Data

NECA responded to the FCC's proposal by requiring certification of final cost study data beginning with 1992 studies.